Transcript

# The Ideas Exchange
# Episode 1: Leaps and bounds - the rise of ETFs
February 2021

Voiceover [00:00:01] Welcome to the monthly Ideas Exchange Podcast, brought to you by ASX - the heart of Australia's financial markets. Each month we'll connect you to a range of leading industry experts who'll give you a look into the finance industry and deliver valuable insights. Hear about important market events, industry research, tips for your own market research, as well as innovative products to help you diversify your investment portfolio.

Voiceover [00:00:34] Your host, Martin Dinh, has a passion for all things investing and is a major player in the investment product game, having assisted in the release of over one hundred and fifty investment products since 2013 with ASX. Join him as he explores investment opportunities beyond just shares from ETFs, REITs, LICs, mFund and much more.

Martin Dinh [00:00:59] Hi everyone. This is Martin Dinh and I'm very excited to bring to you the very first episode of the Ideas Xchange podcast brought to you by ASX. We have a fantastic episode lined up where I'll be joined by my longtime friend and ETF industry expert, Dan Annan, who's the Director and Head of Institutional Business at BetaShares. BetaShares is one of Australia's largest ETF providers, managing over 14 billion dollars in assets and offering 60 ETFs on ASX. In this month's episode, I will chat to Dan about theories of why we think so many people took the investing plunge in the wake of Covid-19, the growing importance of diversification and the rising popularity of ETFs. Dan will then share some tips on what to look out for before buying your very first ETF and some key themes for our listeners to look out for in the ETF space in 2021. So, an exciting first episode lined up. Let's jump right into it with Dan. Hi, Dan, thanks mate for joining me. How have you been?

Dan Annan [00:01:59] I'm doing well mate, and thank you for inviting me. I know you've been working on this project for quite some time, so hopefully we do a good enough job that it keeps you going.

Martin Dinh [00:02:09] Yeah, you know, I'm excited to start this podcast and pumped to record our very first episode. But I actually want to make a special callout, and that someone is BetaShares. I just want to congratulate on BetaShares on hitting the fourteen billion dollars in total assets milestone late last year. When I first started in my role back in 2012, BetaShares was only managing one billion dollars in total assets with only nine products, which I have seen now to grow to sixty ETFs. So it's been a pleasure watching you guys grow over the years. So congratulations to you, Dan, and the team at BetaShares.

Dan Annan [00:02:42] Thank you very much. Definitely, it's been a journey and a testament to sort of the overall market and education and work that the team has put together. Thank you.

Martin Dinh [00:02:53] So, Dan, you've been involved in the ETF industry for over a decade now, so I guess I can call you an ETF industry veteran, if that's OK?

Dan Annan [00:03:03] That's all right. That's all right. You can say that!

Martin Dinh [00:03:05] That's your new nickname. So, for all our listeners out there who are new to ETFs, what is an ETF and what drew you to the ETF industry?

Dan Annan [00:03:15] It's an interesting question. I guess a good way to start. So, first of all, for those of you that haven't heard about an ETF, an ETF is the acronym for Exchange Traded Funds. What drew me to the industry, is one of, I guess, luck. But really, in mid-2000 I was working for an asset manager out in New York and one of our opening of our accounts for an emerging markets fund, the client needed exposure to India and China. Now, I had heard of ETFs in the past. They have been around for quite some time before mid-2000s, but I had never really experienced the usage of them. And long story short, there are certain countries whereby if you open an account, it's quite onerous as far as paperwork. And these countries are called I.D. markets where you need to go through government paperwork, et cetera, to be able to trade physically in those markets. Now, historically, most institutions will use derivatives to access these markets, which can be quite be expensive. But in our analysis, we learn or when we say we learn, the portfolio manager learned that using an ETF will be more efficient for the client. And so that was my first tip toe into an ETF. We were able to use an India and a China ETF for the clients emerging markets portfolio, and that opened my eyes to ETFs.

Martin Dinh [00:04:43] Yeah, that's a really interesting story about what drew you to the ETF industry, and I think my experience is slightly different. I think I was drawn to it as a result, my first ever investing experience. So when I was first starting out in investing, I remember how hard it was to figure out which stocks to buy to build a portfolio. A friend then introduced me to the idea of an ETF. I think I probably owe him a drink or two for that. And now, what stuck out to me about ETFs was that one ETF could hold ten hundreds or even thousands of shares, which as a result could provide me with a diversified exposure to a section of the market, and essentially this was one solution to my investing problem. And now this evidently led me to buy my first ever ETF, which was an ETF that provided exposure or broad exposure to the Australian share market and, Dan, unfortunately it wasn't the BetaShares Australian 200 ETF, because it wasn't around at that time, so don't hate me for that.

Dan Annan [00:05:43] That's OK. I won't hold you to it.

Martin Dinh [00:05:46] But I would, however, like to congratulate you on being the fastest ETF to reach the one billion dollars in total assets milestone though, special congrats there. But anyways, long story short, after seeing firsthand how ETFs have helped me with my investment journey, I guess I knew that my future was in the ETF industry.

Dan Annan [00:06:05] You nailed on the head as to the key reasons why investors are drawn to ETFs. And I talked about a little bit about what they are, but I don't talk about the benefit. Well, a couple of the key benefits of an ETF is you get the benefit of basically using one trade to give you instant diversification. So you were able to get access to the broad market, Aussie share market in the single trade. The ASX has multiple exposures that gives you options to that market. And again, A200, which we launched not too long ago, is one that has given Australian investors the opportunity to access the market at a lower cost.

Martin Dinh [00:06:47] Yeah, I think that it's well summarised and I think that's one of the reasons why I love ETFs and have become an ETF nerd. So, Dan, let's talk investing, 2020 I think was a really challenging year for investors as we saw unprecedented volatility in the markets. In 2020 we saw the S&P ASX 200 was an all-time high in February, only to fall 36% in a space of the month as news of the pandemic broke out. And since then, we've seen the S&P ASX 200 rebound by 45% and now is a few hundred points away from its all time high. Now with all this wild activity going on in 2020. I read an article in the Sydney Morning Herald that four hundred thousand new CommSec accounts were created with a further four hundred thousand users downloading the CommSec mobile app from January

2020 to September 2020. So, Dan, why do you think so many investors decided to suddenly jump into the market despite all this wild volatility in the share market?

Dan Annan [00:07:46] Yeah, look, I think what we saw in March of 2020 basically was an opportunity for investors that have been sitting on the sidelines. As you mentioned, we were at an all high in markets and investors saw an opportunity to basically get in the market. And the question then became, what is the best vehicle for me to use given the current environment? And again, whenever there's some sort of volatility in the market, what are investors looking for? What they're looking for are diversification, transparency, lower cost type exposures to get them set, especially in drawdown periods. And so I think what we saw in March and the growth of ETFs in 2020 was a lot of investors saw an opportunity to be able to put cash to work and take advantage of an historical market drawdown. And again, just think about a lot of these investors also were around in the GFC, right? We also saw, quite interestingly, in 2020 more of a younger generation or millennials getting into the market. And if you take back to 2020 in that time period or the age group or demographic for millennials is now 1980 to 1994 ish. So, they would have been just under 30 this group around the GFC whereby they didn't have enough capital to take advantage in the drawdowns that we saw in 2008 and 2009. In 2020, most of these guys were mid-thirties and forties, have been working for quite some time, have amassed some capital on the sidelines, have been learning quite a bit about the ETF market with all the work that's been put in, put on by the industry and really saw the benefits of being able to access diversification, transparency and liquidity in a single trade, which the ETF tool brings to investors. And not to mention, the tool right now as far as a lot of applications or providers giving investors a tool where they can quickly get access, like, as you mentioned, CommSec. I know BetaShares has worked with CommSec Pocket, whereby one of our funds was selected for the tech sector and NDQ, and we saw quite a bit of flow coming through the CommSec Pocket towards our NDQ product, which covers the the US NASDAQ-100 technology sector.

Martin Dinh [00:10:19] I think, you know, you make a great point. So I kind of took two things away from that. The first thing is with the market so low. So just to give a bit of context, the S&P ASX 200 was at its lowest level in over 10 years. I think, you know, you had some investors out there that were thinking to themselves, hey, this could be that once in a lifetime buying opportunity and I didn't want to miss out on that rebound. And another interesting point that you made there was that, you know, Millennial's was one group of investors that, you know, decided to jump into the market that time. And one of the reasons which I thought was a reason which I can resonate well with, is that, you know, at the time of the GFC, I didn't have the money. But since that time, since the GFC, I've had time to acquire some cash and save money. And then when something like this happened, I had the cash to be ready to invest in, because I didn't want to have the fear of missing out. I didn't want to miss out on that particular rebound. And I think to really highlight this point about taking advantage of this once in a lifetime buying opportunity, in our ASX Investor Study, we found that in the wake of Covid-19, 57% of investors stated that they wanted to invest in Australian shares over the next 12 months. So, I thought that was a really interesting statistic. Another interesting theory that we can share with our listeners is I read a theory from Bloomberg, that they reckon more people decided to jump into the stock market because they had so much free time on their hands and they were trying to find ways to occupy their boredom, with one source of entertainment coming from buying and selling stocks. So, Dan, this theory, and to our listeners, this is theory is called the Boredom Market Hypothesis. Which is essentially an idea that people tend to buy stocks because it's fun, and the more fun stocks are and the less fun everything else is, the more they'll buy stocks. Not going to lie to you, I may be one of those victims of the Boredom Market Hypothesis. And Dan, I think you touched on the point about ETFs being really popular during Covid, you know, it was it was quite volatile and investors turned to ETFs because of their diversification benefits. Dan were there any other aspects of the ETF wrapper, which why investors found ETFs so appealing during the pandemic? Because like just to give our listeners a bit of context. This year, ETFs put in over 30 billion dollars into ASX listed ETFs, which is pretty much 200% higher than the total inflows in 2020. So, I thought, you know, that's quite a remarkable amount of growth. And I think, you know, as an ETF industry expert, why do you think ETFs were so appealing during the pandemic outside of just the diversification benefits?

Dan Annan [00:12:55] Yeah, look, I mean, I think it was a function of timing, ETFs, you know, by the way, like it's been an incredible story and time in and time again, whenever there's volatility in the markets, in every single ETF market that I've been in, and what you see is just tremendous amount of growth. And it's it's been an incredible story for me to witness in the Australian market over the last four years. But really, I think the growth we saw in 2020 was the work that the ETF industry, and in particular BetaShares, is we spent quite a bit of time educating the markets around the benefits of diversification, transparency, lower cost, really thinking about asset allocation and diversification in your portfolios and in a time where a lot of clients and individual investors were turned to working from home and know interesting Boredom Hypothesis, if you want to call it, had a lot of time to look at the EPA and watch markets fall. So, I mean, everyone starts a once in a lifetime opportunity to really invest, right? And again, in this time period, I think you had a lot of investors that had more capital to put to work today that didn't around the GFC. We lived through GFC; we saw the markets drop. The US market dropped approximately 50% over two years in front of our eyes. You Know the GFC was a different systematic issue within the financial markets. The pandemic was totally different, like we were all working from home, but we sort of had the belief that this eventually will be resolved. Right, with the work from central banks really propping up markets with fiscal policy to support those that were unemployed. There was still cash on hand for people shopping online. And so there was there was an opportunity for those that had the means and capital to put money back to work. And I think the ETF industry benefited from those assets because of the work that's been put in by the industry, educating markets around the benefits and the idea of diversification and the idea of transparency. I don't think this this trend is over. I mean, it's really exciting to see the ASX ETF market almost at one hundred billion. And I think we should do that. We should probably hit that number within the next couple of months or so. But we will continue to see that trend of more and more investors really thinking about ETFs as part of their overall portfolio management and professionals as well.

Martin Dinh [00:15:34] Yeah, I think I agree with you on that, Dan. I think when I look at an ETF, you know, I look at, you know, what are the three key benefits? And I think this is something our listeners can kind of take away is the first is that the diversification benefit is transparency and also that it's low cost. But for me, and this is my personal opinion, I think that diversification benefit is the number one benefit. You know, and we actually have some studies that show that is the most important benefit that investors have thought about. So we actually did a survey last year and we found that 31% of the people surveyed in the wake of Covid-19 said they would put greater emphasis on diversification. And, I think this is one thing that could have prompted investors to really move to ETFs because of their diversification benefits. And, you know, when we look at our data, you know, we find that ETFs that provide the most broad exposure to the Australian share market were actually the most popular ETFs in 2020, examples such as a A200, IOZ, STW and VAS, which I really think highlights this trend. So I think that the one thing I'd like our listeners to kind of take away from our chat about ETFs and why investors jumped into the stock market was that, you know, during Covid-19, I think diversification really increased the awareness of actually that investors needed to diversify their portfolio to manage that risk and the volatility and the slump and the vehicle that they can actually turn to manage that diversification was actually the ETF wrapper.

Dan Annan [00:17:11] If you think about it, too, like what diversification gives you in a period of uncertainty and volatility, it gives you some comfort, right. You're not putting all your eggs in one basket. I mean, that's the overall idea, right. And I think you take that same mindset into, OK, do I go out and I own a single technology stock? You know, obviously technology was one of the areas of growth during this pandemic. But do I go out and access one single technology stock or do I think about diversification? And I think that's the ETF wrapper. And the offerings the ASX brings to investors allowed investors to really take advantage of using the ETF as a one wrapper exposure for diversification.

Martin Dinh [00:17:56] Spot on. You actually touch upon an interesting topic, technology. I think, you know, looking at data, you know, we saw the popularity of ETFs grow during Covid. But one area that was hugely popular amongst investors was actually technology ETFs. We found that investors at about one point six billion dollars into technology ETFs in 2020, which was over 600% higher than the total inflows into technology ETFs in 2019. I believe, Beta, you currently offer six technology ETFs and are the experts in this area. So maybe you can provide us with some insights into why technology ETFs were so popular in 2020?

Dan Annan [00:18:34] Yeah, look, I mean, if you think about technology and the implications of Covid, you know, you can put those two together and see why technology became an interesting area of investment. All of a sudden we were all working from home, relying heavily on technology, whether that's communication via technology with the likes of Zoom, if it's work related, Slack, internal communication, shopping online. I'm a technology dinosaur, like always last to the game, right. Because the technology. I'm not joking. Literally, guys in the desk laughed at me when I'm asking questions about technology. But this year I've had to force myself in all the tools that are around me with technology. So a key reason why we saw tremendous growth in technology stocks this year, whether it's Amazon or I won't touch Tesla because that's interesting, or APEN or some of the local names, you know, our way of life really shifted to reliance on technology. And you had all these technology companies that have built their businesses around that. They were also available for trading. And so the question then became like, you know, how do I know which one to buy? Right. And that's why the ETF tool in that sector really allowed investors to take advantage of it. You know, at BetaShares, we've been really, really working hard in ensuring that the Australian investor has the tools at your fingertips to invest and to express their views. And so, you know, as you mentioned, we represent about 50% of the tech sector or tech sector ETFs on the ASX and on the NDQ I think we saw about five hundred or so million net flow in NDQ, which had a tremendous performance for the year from the drawdown of March 3rd. We also have exposure to Asian tigers, which are basically the emerging technology companies like Alibaba, etc. in the emerging world. As well, as you know, we've done a tremendous job working with the ASX and really bolstering the technology sector. And we've partnered with ASX and the S&P to deliver the technology sector and the ETF for Australian investors ATech. So all combined we saw about, I think, of all the flow into technology and on the ASX and BetaShares has represented about 80%. And that's a testament to the work that the team has been doing, really educating the market around the tools that they have available at their fingertips to express their views. But the driver of, you know, to close that sort of conversation, the driver of growth and technology, really had to do with the way Covid changed the way we live. Society basically shifted their reliance towards technology in a massive way. And I think we will continue to see that and we'll continue to see more meetings on Zoom. You continue to see more communication via Slack. You will continue to see more shopping online. It's a convenience and it's a positive convenience way of life. And that's what technology brought to the table.

Martin Dinh [00:21:50] Yeah, I think this year's been dealing with Covid, and like you, I'm a technology dinosaur as well. Quite terrible with technology. But working from home, it's made me ever increasing reliance on things such as video conferencing, online shopping and online entertainment. I think, you know, many people were in the same boat as well, right. And investors probably, you know, when they've seen something like this happen, they were like, I want to find the best way to ride this tailwind. And I think, you know, you mentioned this before about, you know, investors who are unsure of which individual technology companies to choose from. Maybe they wanted to get exposure to the technology sector instead. And that's when the ETF became a useful tool for these investors, which I think to me is a is a really key takeaway for our listeners today that, you know, ETFs can be used as an investment tool to express a view on a particular theme, such as the technology sector. Now, Dan, continuing on the topic of ETFs, we found that there was quite a few number of investors buying ETFs as their first investment, with our ASX Investor Study, showing 8% chose ETFs as their very first investment. Now, Dan, as an ETF veteran, what are some tips that you can share to our listeners before buying into an ETF?

Dan Annan [00:23:09] Yeah, it's a great question. Look, I think one of the key things is that make sure you do your homework again. So, what does an ETF? An ETF is a collection of securities representing an index, that's wrapped into a single stock. Most providers have, and at least at BetaShares, we have our holdings available to you online where you can actually see what you own. So, it's important that you do your homework and understand the exposure that you're getting within that wrapper. So, I think that's the key. So now, one, you want diversification, you made a decision that you want a specific exposure, but do a little bit of homework to ensure that, you know, the exposure that you think you're getting is exactly what you're getting. The other thing is, for first time investors, because these products trade just like shares on an exchange, remember, you're buying into a collective underlining that's wrapped into a single stock on the exchange. So you have to think about the most efficient way of trading. What I would encourage those that are sort of starting new or even if you haven't already, but I encourage you to do is really think about the order types that's available to you. I spent my time working with institutional investors that are buying ETFs, and I spent a lot of time just really talking about order types. And for the most part, depending on the size they're looking to do, we try and work with them on limit orders. A market order and a limit order. If you if you look on screen, the price that you're seeing on screen, whether fair or not, is what the market makers and the market is pricing, right. If you put in a market order, basically you are you a price taker, in essence. That's well and good. But I would encourage you to really think about limit orders. Depending on the size you're looking to trade, you may not get your trade size done. This is where, depending on the size that you're looking to trade, most providers have the capital markets desk that can help guide you. So I would encourage you, at BetaShares, you know, we do have a capital markets team that can help guide you and how you trade. And in addition to that, we have plenty of resources on our website that you can go and get smarter. So, on our website, we have an education centre where we produce one on one content to allow beginners to really understand the ETF structure, the exposures, the trading of those exposures. So if I leave you with anything, the two tips are, one, know what you own, so do a little bit of homework to understand what you own and then when it comes to trading, just think about the limit orders.

Martin Dinh [00:25:49] That's well summarised. I think the limit order point is something that listeners can really take away from because, you know, especially when markets are quite volatile. If you put in a market order and the market's moving so fast, you might get hit at a price that you might not want. But if you have a limit order, you can specify what price you want to set, your buy and sell price. So I think that's really important. And I think for me, when I make an investment decision, I think looking under the hood is probably the number one.

And really, I can just give you an example. We have two ETFs currently on the ASX under the ASX code RARI and FAIR. You know, they both look similar on the surface. You know, they look to invest in companies on the ASX and filter out companies that don't meet environmental, social and governments criteria, with RARI tending to favour companies that pay high dividends. So, you know, they look similar. But, you know, when we actually look under the hood, we find that RARI actually has a higher allocation to companies in the financial sector, whilst FAIR has a high allocation to companies in the health care sector, which is likely due to RARI favouring higher dividend paying companies. And really, as a result of this different sector allocation, the returns were materially different. I think this is the one of the many examples of why it's so important to look under the hood. So, again, Dan, well summarised and I hope our listeners take away those two tips, use limit orders and make sure you look under the hood.

Dan Annan [00:27:10] Look, I want to actually want I want to tap on that. Just touch on that a little bit. You bring up an interesting example, which is the two ETFs that you bring up are ESG ETFs, which are basically values, values alignment. Like my values might be different from your values. Right. And now just outside of looking at performance and looking at sort of sector allocations, et cetera, you know, in particular when you're talking about ESG, make sure that your values aligns with the definition of the values of the exposure, because that's a really interesting segment when it comes to ESG whereby, you know, you can ask 10 different people in a room what their preference for ESG is and you'll get 10 different answers, and one of the things at BetaShares that we've done in this segment is just to try and answer that question to the common denominator, when it comes to ESG. So for those looking for ESG exposures, I think it's very, very important that you really flip the hood, take a look at the underlying companies that's under the hood. But more importantly, take a look at the definition of criteria for those values, right. At BetaShares, we sort of, we took what I would call a hard cut to if you're sort of if you're like in a spectrum of like light green, dark green with dark green being really harsh on the E the S and the G, we went dark green. Right. There's no ambiguity as to the E the S energy in our exposures. Whereby, you may have some investors that want to be benchmark aware, which would mean that you would need to sort of go a little bit lighter on that green to gain a benchmark aware exposure. So again, this is one of those key example that you bring up around flipping under the hood to ensure that what you're buying is what you want.

Martin Dinh [00:29:10] Yeah, but that's the reason why looking under the hood is so important, and I hope, you know, that's something that you really take away and especially use that as an important point when you first jump into your investment journey. Now, Dan, a final question for you. I'm looking to the future and you know, no one's got a crystal ball, so we won't hold you to it. What sort of areas should our listeners look out for in 2021?

Dan Annan [00:29:34] There's a few things. I mean, one of the things, it's not like we flipped into 2021 and all the themes that were sort of happening in 2020 went away. Right. Covid-19 is still an issue today. Today we have vaccines and there are plans to manage that down the road. And so hopefully as more people get vaccinated, we should see less and less of people catching the virus and hopefully allowing all of us to sort of get back to the new normal, whatever that that looks like. So the themes that sort of rode into 2020, I still see sort of that happening in 2020. So technology, that's still going to be an area of consumption and reliability by all of us. Right. And so that's going to be an interesting space. Another area with the new president, the 46th president of the US coming in play, to think about, would be what he's going to do with some of the policies put in place by the previous president. So things like, you know, trade wars, like we see that sort of dying down a bit. This morning I flipped my news and he's already started reversing about 15 of those policies. One thing that we've all heard quite a bit is getting the US back into the Paris Accord. That's an ESG theme, right? ESG was a big theme going into 2020. And then we had covid-19 sort of come about and sort of muted that conversation a bit, especially in Australia. We had the bushfires going into 2020 and then we had Covid-19. There was a lot of talk around ESG and the beginning of 2020 and that sort of muted with Covid. So, I think you will see more of that conversation pick up, especially with companies, global governments really thinking about a net zero carbon environment by mid-century. And so ESG is going to be a theme in this market in 2020. And I would encourage you to do your research and learn what's out there and what's appropriate for you for an investment. And last but not least, because we are all heavily reliant on technology today, cyber security is going to be an interesting space because you would expect that because we're all relying on technology, we will have some challenges around being hacked, et cetera. And to that end, companies that provide services to protect cyber hacks will benefit and grow in this environment. So, I think we recently published our 2021 outlook on our website. It's presented by Chief Economist, and it's available for you to go out and have a look. But we think there's an opportunity to really think about the tech sector, the ESG sector, particularly within the tech sector, thinking about cyber security. And we an ETF that covers all those asset classes.

Martin Dinh [00:32:39] 2021 looks like it's going to be quite a year for us cyber security, technology and ESG. Well, Dan, that's a wrap. Thank you for joining us and providing our listeners with some wonderful insights into the ETF space. I really enjoyed our chat and hope our listeners found this information useful. We look forward to welcome you back down the road.

Dan Annan [00:32:58] Thank you very much.

Martin Dinh [00:33:00] Well, that concludes the first episode of the Ideas Exchange Podcast. I hope you have enjoyed it as much as I did and learnt about some things such as the importance of diversification in the wake of Covid-19 and ETFs as a useful investment tool to help you build a diversified portfolio. Next month, we have an exciting show lined up where I'll be joined by industry veteran, Gemma Dale, director of S, an investor behaviour at Nab Trade, as we explore an area that we are both passionate about, the importance of investing for women. Thanks for listening.

Voiceover [00:33:33] Visit the ASX website ASX.com.au and register for the next Investor Day, our premier education event providing timely market insights and ideas from a range of industry experts.